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# SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1946

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LILLIAN JEFFRIES,

Petitioner,

versus

COMMISSIONER OF INTERNAL  
REVENUE,

Respondent.

## PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

TO THE HONORABLE THE CHIEF JUSTICE AND  
ASSOCIATE JUSTICES OF THE SUPREME COURT OF  
THE UNITED STATES:

This is a petition for a writ of certiorari to review  
the decision of the United States Circuit Court of Appeals  
for the Fifth Circuit.

### JURISDICTION

Jurisdiction of this Court is invoked under Section  
240 (a) of the Judicial Code as amended by the Act of  
February 13, 1925, c. 229, Sec. 1, (43 Stat. 938). (United  
States Code, Annotated, Title 28, Sec. 347). The decision

sought to be reviewed was rendered on November 22, 1946, and application for rehearing, seasonably made and entertained by the Court, was denied on December 24, 1946.

### QUESTIONS PRESENTED

This case came to the Circuit Court of Appeals upon a petition for review of a decision of the Tax Court of the United States, which determined a deficiency in income tax of Lillian Jeffries in the sum of \$32,827.36 for the year 1940 (R. 30).

The respondent, Commissioner of Internal Revenue, on May 2, 1944, served upon the petitioner, Lillian Jeffries, a notice of deficiency, (R. 10) who in turn duly filed with the Tax Court of the United States her petition for redetermination of the deficiency (R. 2). Answer was filed by the Commissioner of Internal Revenue, (R. 15) and in due course the cause came on for hearing before Honorable Arthur J. Mellott, one of the Judges of said Court, then and there presiding at Miami, Florida. Thereafter, on December 28, 1945, the Tax Court of the United States promulgated its findings of fact and opinion, and on December 29, 1945, its decision determining the deficiency was entered (R. 16, 29). Thereafter, on March 13, 1946, the petitioner filed her petition for review by the Circuit Court of Appeals (R. 30). The Circuit Court of Appeals on November 22, 1946, affirmed the decision of the Tax Court of the United States, (R. 40) and on December 24, 1946 denied rehearing (R. 58).

The facts upon which the deficiency is alleged to have arisen are, briefly, as follows:

Girard Realty Company was originally organized by J. B. Jeffries, William L. Austin and a third person for the purpose of acquiring and holding title to a large tract of undeveloped lands in the Everglades section of Florida (R. 18).

Many years ago, and prior to 1932, a portion of the lands was disposed of and the corporation reorganized and continued for the purpose only of holding title to said lands. Upon the reorganization J. B. Jeffries and William L. Austin each owned fifty per cent of the capital stock of the corporation. In 1932 Austin died, and in 1936 Jeffries died. The Executors of the Austin Estate succeeded to the stock owned previously by Austin, and Mrs. Jeffries succeeded to the stock owned previously by her husband. (R. 18).

The corporation did no business and had no income, but on the contrary it was necessary from year to year for Austin and Jeffries to personally contribute the funds necessary to pay State, County and Drainage District taxes. After the death of Austin and Jeffries these taxes were not paid as they became due, and finally in 1939 there was a large accumulation of unpaid State, County and Drainage District taxes. The property was about to be lost for taxes. Mrs. Jeffries called upon the Austin Estate to contribute one-half of the money necessary to redeem the lands from tax sale. The Austins refused, and Mrs. Jeffries advanced the money for the purpose of paying the taxes, taking mortgages on the property of the company to secure the sums so advanced. A dispute arose between Mrs. Jeffries and the Austins and she began foreclosure of her mortgage. Whereupon the heirs and

executors of the Austin Estate intervened in the foreclosure and had themselves made parties defendant and the case thereupon proceeded as a suit between Mrs. Jeffries and the executors and heirs of the Austin Estate. (R. 18, 19).

The Austins in their pleadings charged Mrs. Jeffries with fraud, and considerable feeling arose between the parties to the litigation. Finally a settlement of all of their differences was agreed upon between Mrs. Jeffries and the Austins. It was agreed that a portion of the property would be sold for the purpose of securing the funds with which to reimburse Mrs. Jeffries for her advances and for the payment of attorneys and auditors, and that all of the remaining assets of the corporation would be equally divided between the two stockholders—Mrs. Jeffries and the Austins. An agreement embodying the terms of the settlement was prepared, signed by Mrs. Jeffries and forwarded to Philadelphia to be executed by the Austins. A sale was consummated of a portion of the lands which it was agreed would be sold, and the parties met for the purpose of putting the settlement into effect. At that meeting the Austins stated that their Estate was still in the process of administration and they had no one who could take title to the half of the property being allocated to them, and requested Mrs. Jeffries to accept deed to her half of the property, surrender her stock in the corporation, and allow the Austins to retain title to their half of the property being received in the settlement, in the name of the corporation. Mrs. Jeffries was suspicious of consummating the settlement and refused to permit it to be done in that way. However, upon assurance of her own attorneys and an income tax expert that this method

of handling it in no way changed her legal or income tax status, she consented for the matter to be handled in that way. The net result was that the assets of Girard Realty Company were equally divided between Mrs. Jeffries and the Austins, Mrs. Jeffries taking title to her half in her own name and the Austins retaining the title to their half in the name of Girard Realty Company. The lawsuit was settled and dismissed and the Austins executed releases exonerating Mrs. Jeffries of the charges which had been made against her in the litigation (R. 19, 20, 21).

Mrs. Jeffries thereupon caused the lands received by her in the settlement to be appraised by an appraiser for the Federal Land Bank. She believed that the appraisal so made was inadequate and she voluntarily increased the appraised value of the property to a much higher figure (R. 24).

Mrs. Jeffries thereupon reported as income for 1940 the difference between the amount which she had paid at a "wash sale" of her stock and the value of the property as fixed by her, which was an amount greatly in excess of the appraised value of the property. She reported this as a long term gain and promptly paid her taxes on it in the sum of \$18,169.47 (R. 24, 25, 11). Thereafter the Commissioner of Internal Revenue served notice upon Mrs. Jeffries of an alleged deficiency in her tax for 1940, based upon the contention that the gain realized by her in the acceptance of said property was a short term gain rather than a long term gain, because, as he contended, the property had been received by her in partial liquidation of the corporation (R. 10, 12, 25). The issues submitted to the Tax Court of the United States were these:

Respondent contended that because Mrs. Jeffries surrendered her stock and accepted a deed to her half of the property, whereas the Austin Estate retained title to their half in the name of the corporation, the transaction constituted a partial liquidation of a corporation and was taxable under the provisions of Section 115(c) of the Revenue Act of 1938 (then in effect, but since repealed) as a short term gain. (R. 12, 25).

The petitioner contended that the transaction was an equal division of the assets of the corporation between herself and the Austin Estate in settlement of a lawsuit and was not a partial liquidation of the corporation; that the division was complete, and that each stockholder received one-half of the assets of the corporation; that the fact that the Austins permitted their half of the property to remain in the name of the corporation did not alter or change the effect (R. 25, 26).

Petitioner contended that Section 115(c) aforesaid was intended by Congress to cover only ordinary dividends distributed under the guise of distributions in partial liquidation and that Congress never intended said Section to apply to unquestionable bona fide redemptions of stock not equivalent in any way to the distribution of a taxable dividend; and that said Section did not apply to the division of assets which was accomplished by the transaction here under consideration (R. 25, 26).

Petitioner contended that the entire transaction must be considered and the net results obtained must determine the character of the transaction, and that the component parts of the transaction could not be considered separate-



ly for the purpose of determining its character, and that substance, rather than form, should control (R. 27).

Petitioner contended that her gain (enhanced value of the property received) was a long term gain and taxable as such, and that since she had paid the full amount of taxes chargeable on that basis, the alleged deficiency should be disallowed (R. 24).

Following the determination of the deficiency by the Tax Court of the United States, the petitioner filed with the Circuit Court of Appeals her petition for review, assigning as errors the following acts and omissions of the Tax Court of the United States:

1—The findings of the Tax Court of the United States that there was a partial liquidation of Girard Realty Company.

2—The refusal of the Tax Court of the United States to consider the intent of the parties and to give effect to that intent in construing the effect of the transaction whereby Petitioner received one-half of the assets of Girard Realty Company.

3—The finding of the Tax Court of the United States overruling and denying the contention of Petitioner that the provisions of Section 115(c) of the Revenue Act of 1938 (since repealed) were intended by Congress to apply only to the distribution of taxable dividends disguised as distributions in liquidation, and did not apply to bona fide redemptions of stock.

4—The findings of the Tax Court of the United States whereby it construed only the fact that Petitioner surrendered her stock in Girard Realty Company and received one-half of its assets, and refused to consider the entire transaction and give effect to the intent of the parties, which was that there should be a complete division of the assets of the corporation between two groups of stockholders.

5—The finding of the Tax Court of the United States that the capital gain realized by Petitioner in receiving one-half of the assets of Girard Realty Company constituted a short term gain.

6—The finding by the Tax Court of the United States that there is a deficiency of \$32,827.36 in the income tax of Petitioner for the year 1940.

7—The making an entry by the Tax Court of the United States of its Decision of December 29, 1945 (R. 33, 34).

The Circuit Court of Appeals affirmed the decision of the Tax Court of the United States. This petition for certiorari follows.

### REASONS FOR ALLOWANCE OF WRIT

It is respectfully submitted that certiorari should be granted in this case for the following reasons:

1. The present decision is in conflict with the decisions of other Circuit Courts of Appeal and with other decisions of the same Circuit Court of Appeals.

2. The Circuit Court of Appeals has herein decided a federal question in conflict with applicable decisions of the Supreme Court of the United States.

3. The Circuit Court of Appeals has herein decided an important question of federal law which has not been, but should be, settled by the Supreme Court of the United States.

4. The Circuit Court of Appeals has overlooked and failed to pass upon certain essential assignments of error.

5. The Circuit Court of Appeals has misunderstood, and therefore mis-stated, certain essential contentions of the Petitioner.

## SUPPORTING BRIEF

### General Justice and Equity

In the Majority Opinion the Circuit Court of Appeals said (R. 42):

"Whether a transaction or result is taxable, and what the tax is, is not a matter to be determined in law upon considerations of general justice or equity."

The Majority Opinion in this case is in direct conflict with the pronouncement of the same Court in the case of **Alamo National Bank of San Antonio vs. Commissioner of Internal Revenue**, 95 Fed. (2d) 622, where the court after holding that taxation is a matter of statutes and equitable considerations cannot override the provisions of the statute, nor always supply their omissions, said, (page 623):

"Nevertheless, honesty, good faith, and consistency are due in tax accounting. The right and wrong of things, and equitable principles have a place in tax matters."

The pronouncement in this case, as above quoted, is also in conflict with the decision of the Supreme Court of the United States in the case of **Stone vs. White**, 301 U.S. 532, 81 L. Ed. 1265, 57 S. C. 851, where that court not only recognized equitable pleas, but based its decision upon equitable considerations, and on page 1271 of 81 L. Ed., the court in reaching its conclusion said:

"Equitable conceptions of justice compel the conclusion that the retention of the tax money would not result in any unjust enrichment of the Government."

### **Repeal of Act**

The Circuit Court of Appeals overlooked and failed to pass upon Petitioner's Assignment of Error No. 3, (R. 34) wherein Petitioner assigned as error:

"The finding of the Tax Court of the United States overruling and denying the contention of Appellant that the provisions of Section 115(c) of the Revenue Act of 1938 (since repealed) were intended by Congress to apply only to the distribution of taxable dividends disguised as distributions in liquidation, and did not apply to bona fide redemptions of stock."

In the Majority Opinion the Court said (R. 42):

"Neither will it avail her to point to the fact that Congress in 1942, recognizing the inequities of Section 115(c), repealed the provision taxing a partial liquidation as a short term gain, without making the repeal retroactive."

The Court appears to have misunderstood the contention of the Petitioner and appears to have believed that Petitioner contended that Section 115(c) should be disregarded because it has since been repealed. This was not the contention of Petitioner, as set forth in the Assign-

ment of Error No. 3 nor does it follow Question No. 1, as set forth in the questions for determination in the Petition for Review (R. 32). The question as presented in the Assignments of Error and the Petition for Review is that it never was the intention of Congress that the provisions of Section 115(c) should apply to bona fide redemption of stock, but that it was the intention of Congress, as reflected by the reports of legislative committees filed at the time of its repeal, that the provisions of this Section should apply only to distributions of taxable dividends disguised as distributions in liquidation.

In 1942 the Congress recognized the injustice of Section 115(c) of the Revenue Code and eliminated it as to taxable years subsequent to 1941. The Senate Finance Committee, in its report on the Revenue Bill of 1942 (Report No. 1631, to accompany H.R. 7378, filed October 2, 1942) on page 116 thereof, in dealing with this Section, said:

"This treatment was occasioned by the facility with which ordinary dividends may be distributed under the guise of distributions in partial liquidation, although Section 115(g) makes explicit provision for the treatment of such distributions as ordinary dividends. Inequality results, however, under the existing law in the case of unquestionable bona fide redemptions of stock not equivalent in any way to the distribution of a taxable dividend. It is believed that the proper application of Section 115(g) will prove adequate to prevent taxable dividends disguised as liquidations from receiving capital-gain treatment. Accordingly, this Section of the Bill eliminates the pro-

vision requiring the gain from a partial liquidation to be treated as a short-term capital gain."

This Petitioner has never contended that the mere repeal of a section of the statutes, regardless of its inequity or unreasonableness, would have a retroactive effect. On the other hand Petitioner contended both in the Tax Court and in the Circuit Court of Appeals that in determining legislative intent the Court could and should consider the solemn declarations of Congressional Committees, including those filed with the repeal of the Section; it was the further contention of Petitioner that the statement set forth in the legislative committee's report is a clear and unmistakable statement that Congress never did intend that this Section should apply to bona fide redemptions of stock.

### **Intention of Parties**

The Circuit Court of Appeals misunderstood and therefore mis-stated the contention of the Petitioner with respect to the effect to be given to the intention of the parties, as set forth in Assignment No. 4 of the Assignments of Error (R. 34).

In the Majority Opinion this Court said (R. 42):

"Because the statutes and regulations read as they do, and the facts are what they are, it will not avail Petitioner to point (1) to the fact that she all along intended to bring about a complete liquidation, and that she regarded the course taken as bringing this about."

Petitioner has never contended that the result of the action taken should be determined solely upon what "she all along intended."

Petitioner's Assignment of Error No. 4 charges as error:

"The findings of the Tax Court of the United States whereby it construed only the fact that Appellant surrendered her stock in Girard Realty Company and received one-half of its assets, and refused to consider the entire transaction and give effect to the intent of the parties, which was that there should be a complete division of the assets of the corporation between two groups of stockholders."

It was the contention of Petitioner that it was the intention of both parties to the transaction that there should be an equal division of the property of the corporation between the two groups of stockholders, and that this was actually accomplished.

It is clear from the Findings of Fact and as reported by the Tax Court that there was a complete distribution of all of the assets of Girard Realty Company; one-half to Mrs. Jeffries and one-half to the Austins. It was not a partial distribution. The distribution was complete and included all of the assets of the Company.

The fact that Mrs. Jeffries took title to her half in her own name, and the fact that the Austins left the title to their half in the name of the Company does not alter



the fact that Mrs. Jeffries got half of the assets and the Austins got the other half. There can be no doubt that what the parties had in mind was to dissolve their relationship and divide their property between them.

Judge Mellott of the Tax Court correctly stated this proposition when he said (R. 29):

"The net effect, therefore, was a complete division of the assets of the corporation between the two groups of stockholders."

In reaching its conclusion the Circuit Court of Appeals undoubtedly also overlooked that provision in the Resolution adopted by the Corporation, wherein the Corporation stated (R. 24):

"It being further resolved that the payment of the monies and the issuance of the deed, as in this Resolution referred to, be and the same are hereby determined to have been made for the purpose of liquidating and dividing the assets of this Company."

Petitioner is fully aware that in determining the intent of parties to a contract the intention of one of the parties alone would not be sufficient. This Petitioner, therefore, never has contended that her intent standing alone would be sufficient to determine the effect of the transaction. What she did contend is that it was the intention of both parties to the transaction that there should be an equal division of the assets of the Corporation between the two stockholders, and that this actually was accom-

plished regardless of the mechanics adopted in its consummation.

### **Hardship**

The Circuit Court of Appeals misunderstood and therefore mis-stated this Petitioner's contention when the Court said, in the Majority Opinion (R. 42):

"It will not avail Petitioner to point \* \* \* to the tax hardships she is being subjected to for a mere mistake in method if the method adopted is found to be a mistaken one."

This Petitioner has never contended that the "hardships she is being subjected to" is a sufficient ground for the reversal of the decision of the Tax Court. The Court's statement leaves the erroneous impression that Petitioner has appealed merely for sympathy and has not based her case upon sound considerations of the law.

### **Substance vs. Form**

In the Majority Opinion the Circuit Court of Appeals held that whether a transaction or result is taxable, and what the tax is (R. 42)

"is a matter of statutes and valid regulations, and what they mean. Neither is it to be determined in fact upon considerations of what was intended to be done. Rather it is to be determined by what was done. \* \* \* Taxation deals not with what was attempted to be done but with what was done."

Under the facts and the contentions of Petitioner in this case, the ruling of the Court above quoted is tantamount to a ruling that the tax liability will be determined solely upon the form and mechanics adopted in the transaction, and that neither the intent of the parties nor the effect of the action, or the results actually accomplished will be considered.

Such a ruling is in direct conflict with the decision of the Circuit Court of Appeals of the Sixth Circuit in the case of **Mather vs. Commissioner**, 149 Fed. (2d) 393; the decision of the Circuit Court of Appeals of the Tenth Circuit in the case of **Prairie Oil & Gas Co. vs. Motter**, 66 Fed. (2d) 308 and the decision of the Supreme Court of the United States in the cases of **Corliss vs. Bowers**, 281 U.S. 376, 74 L. ed. 916, 50 S. C. 336, and **Minnesota Tea Co. v. Helvering**, 302 U.S. 609, 82 L. ed. 474, 58 S. C. 393.

The effect of the four decisions cited, as well as other cases not cited, is that "the substance of the thing done and not the form it took, must govern, and the courts have recognized that where the essential nature of a transaction is the acquisition of property, it will be viewed as a whole, and closely related steps will not be separated either at the instance of the taxpayer or the taxing authority" (149 Fed. (2d) 393, 397).

The effect of that part of the decision of the Circuit Court of Appeals in the present case, above quoted, is to hold that because the form adopted in one step in the transaction conforms to the definition of a partial liquidation, all other steps, as well as the intentions of the parties and the actual results accomplished, are to be ignored.

The above quoted portion of this decision is in conflict with the decision of the Supreme Court of the United States in **Corliss vs. Bowers**, 281 U.S. 376, 74 L. ed. 916, 50 S. C. 336, wherein the Supreme Court on page 917, L. ed. said that

“taxation is not so much concerned with the refinements of title as it is with actual command over the property taxed—the actual benefit for which the tax is paid,” \* \* \*

It makes no difference that such “command” may be exercised through specific retention of legal title or the creation of a new equitable but controlled interest, or the maintenance of effective benefit through the interposition of a subservient agency. As was most aptly stated in **Minnesota Tea Co. vs. Helvering**, 302 U.S. 609, 82 L. ed. 474 at page 477, 58 S. C. 393,

“a given result at the end of a straight path,  
\* \* \* is not made a different result because  
reached by following a devious path.”

In the present case, the “given result at the end of a straight path” was the acquisition by the Austins of a half of the property; and this result was not changed by the fact that title remained vested in a corporation owned exclusively by them. When Mrs. Jeffries surrendered her stock Girard Realty Company became the mere trustee or repository of the legal title for the lands of the Austins, who were the owners of the beneficial interest. Leaving title in the name of a company exclusively owned by the Austins was just a convenient method of handling it, and

the company thereupon became the repository of the title for them until such time as they decided to sell. The result was the same as if they had caused the title to be vested in some other corporation which they owned.

The following facts were reported by the Tax Court of the United States in its Findings of Fact (R. 21):

"The Girard Realty Co. was not a party to the negotiations between Petitioner and the Austins for the division of the land held by it. The settlement was arrived at by the parties in interest as a division of the property to which the company held title and as a settlement of the foreclosure suit which had been instituted by Petitioner."

We submit that the true rule was stated in the dissenting opinion of Judge Mellott of the Tax Court, where he said (R. 28):

"While I recognize the fact that the mechanics adopted point strongly to a mere partial liquidation of the corporation, actually what occurred was a division of the assets of the corporation in kind, the Austins engineering the whole plan for the purpose of making use of the corporation as the nominal title holder for the portion of the property distributed to them."

We respectfully submit that the Circuit Court of Appeals in the Majority Opinion overlooked this contention of the Petitioner and failed to pass upon the question thus raised.

## CONCLUSION

The Circuit Court of Appeals rendered its decision by a divided court. That there was a wide divergence of opinion among the members of that court is clearly shown by the forceful, single sentence dissenting opinion by Judge Waller (R. 43):

"Regardless of the insatiability of Taxation's appetite and the present emptiness of her voracious maw, the courts ought not to try to satisfy one and fill the other by upholding extortions from inexperienced widows when such could be, and should be, avoided by following the salutary rule of looking at the substance of the transaction rather than at its form."

Substance rather than form should control, and the equities of the case should be considered. For the reasons hereinabove set forth, we respectfully ask that this Court grant a writ of certiorari to bring before this Court for review the decision of the Circuit Court of Appeals.

Respectfully submitted,

LILLIAN JEFFRIES

Petitioner

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**In the Supreme Court of the United States**

OCTOBER TERM, 1946

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**LILLIAN JEFFRIES, PETITIONER**

**v.**

**COMMISSIONER OF INTERNAL REVENUE**

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**ON PETITION FOR A WRIT OF HABEAS CORPUS TO THE UNITED  
STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH  
CIRCUIT**

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**BRIEF FOR THE RESPONDENT IN OPPOSITION**

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# **In the Supreme Court of the United States**

OCTOBER TERM, 1946

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No. 1000

LILLIAN JEFFRIES, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

---

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED  
STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH  
CIRCUIT*

---

**BRIEF FOR THE RESPONDENT IN OPPOSITION**

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## **OPINIONS BELOW**

The opinion of the Tax Court (R. 16-28) and its dissenting opinion (R. 28-29) are reported at 5 T. C. 1338. The opinion of the Circuit Court of Appeals (R. 39-42) is reported at 158 F. 2d 225.

## **JURISDICTION**

The judgment of the Circuit Court of Appeals was entered on November 22, 1946. (R. 42.) A petition for rehearing (R. 43-55) was denied on December 24, 1946 (R. 56). The petition for a writ of certiorari was filed on February 10, 1947.

The jurisdiction of this court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

#### QUESTION PRESENTED

Whether a distribution in 1940 of corporate assets to taxpayer in complete cancellation of one-half of the corporation's stock was a distribution in partial liquidation, as defined in Section 115 (i) of the Internal Revenue Code, with the result that the gain on the distribution was includible in taxpayer's income in its entirety under Section 115 (c) of the Code.

#### STATUTE AND REGULATIONS INVOLVED

The applicable statute and Regulations are printed in the Appendix, *infra*, pp. 15-18.

#### STATEMENT

The facts found by the Tax Court (R. 17-25) may be summarized as follows:

The Girard Realty Company (hereinafter referred to as "corporation") was organized to own and sell lands in the Everglades section of Florida. Prior to 1932 its 25 shares of common stock were owned equally by taxpayer's husband, J. B. Jeffries, and by William H. Austin. In 1932 Austin died and his estate, which was administered in Pennsylvania, succeeded to the 12½ shares owned by him. (R. 18.)

In 1936 Jeffries died and in 1937 the taxpayer acquired the 12½ shares of stock formerly owned

by him. Both the taxpayer and the Commissioner have accepted \$2,750 as her basis for computing gain or loss on disposition of the stock. (R. 18.)

From 1936 to 1940, the assets of the corporation consisted of undeveloped lands which were held for sale, but none of which were sold during this period, although 55,000 acres had been disposed of prior to 1932. Some rent was received during the period but it was not sufficient to pay taxes on the land. (R. 18.)

After 1937 taxpayer was president of the corporation and manager of its affairs. The Austin estate did not maintain representation on the board of directors or among its officers. Prior to 1940, taxpayer asked for contribution from the Austin estate to pay accumulated taxes against the lands which the corporation had no funds to pay, but the estate refused to contribute. Taxpayer then advanced the money to pay the taxes and took mortgages on the corporation's property to secure the amounts advanced. (R. 18-19.)

On January 24, 1940, the taxpayer filed a suit to foreclose the mortgages and on February 5, 1940, a decree *pro confesso* was entered against the corporation. On the same day the Austin estate and heirs petitioned for, and on February 19, 1940, were granted, leave to intervene, and the decree was vacated. Among other things, the Austin estate alleged in its answer that the taxpayer had been guilty of fraud and that the mortgages were not valid. It requested that an

accounting be had and that a receiver be appointed to manage and control the corporate affairs for the purposes of liquidating the assets of the corporation, paying its indebtedness, and protecting the interests of stockholders. (R. 19.)

Thereafter, negotiations for settlement of the litigation were entered into by taxpayer and the Austin estate, and on March 27, 1940, they signed an agreement settling the issues. The agreement provided for sale of some lands to raise funds to pay expenses of the litigation and the amount advanced by taxpayer for payment of taxes; recited that it was desirable to effect a fair division of the remaining lands of the corporation among the stockholders; and that the parties would attempt to arrive at an agreed plan for a fair division before settlement day. As originally drafted the agreement provided for complete liquidation of the corporation, but representatives of the Austin estate redrafted it, inserting a provision that the corporation should not be liquidated completely or dissolved; that the lands allocated to the Austin estate should not be transferred to it, except as it requested; but that this did not qualify or limit the right of taxpayer to have distributed the lands allocated to her upon surrender to the corporation of the stock held by her. (R. 19-20.)

The taxpayer at first refused to sign the agreement as redrafted, because she understood that there was to be a complete dissolution of the cor-

poration. Upon being assured by attorneys and an income tax advisor that the retention of the corporation by the Austin estate would not affect her legal or income tax status, she executed the agreement. (R. 20-21.)

The corporation was not a party to the negotiations between the taxpayer and the Austin estate for the division of its lands. The settlement was made by the stockholders as a division of the property to which the corporation held title and as a settlement of the foreclosure suit. On April 3, 1940, the foreclosure suit was dismissed by court order pursuant to stipulation. (R. 21.)

At a meeting of the board of directors of the corporation on April 4, 1940, resolutions confirming the settlement were adopted. The minutes set out an involved accounting, the effect of which was that taxpayer and the Austin estate each received \$12,951.69 in cash or property; the attorneys and auditors received \$12,201.62; taxpayer was reimbursed for advances aggregating \$22,181.27; and she received one-half of the remaining lands of the corporation, having a value of \$87,802. The Austin estate became entitled to receive the other half of the lands having approximately the same value. The title to the lands not transferred to taxpayer remained in the corporation. (R. 21-22.)

A resolution adopted at the meeting provided for the issuance to taxpayer of a warranty deed

to such lands of the corporation as she should direct, provided she delivered to the corporation a written statement from the Austin estate agreeing that the lands so demanded were a fair division of the corporation's lands. It was resolved that upon issuance of the deed taxpayer should surrender to the treasury of the corporation for cancellation the  $12\frac{1}{2}$  shares of stock held by her, and the consideration for issuance of the deed was in exchange for the surrender and cancellation of the stock held by taxpayer. It was further resolved that the cash amounts of \$12,974.80 paid to taxpayer and to the Austin estate were determined to be a return of capital investment and in no sense to be considered a dividend out of profits. Finally it was resolved that the money payments and the issuance of the deed were determined to have been made for the purpose of liquidating and dividing the assets of the corporation. (R. 22-24.)

Taxpayer received a deed from the corporation for the portion of the property she was to receive under the agreement with the Austin estate and surrendered her  $12\frac{1}{2}$  shares of stock to the corporation. (R. 24.)

In her income tax return for 1940 the taxpayer reported the gain on receipt of the property transferred to her as a long-term capital gain, 50 percent of which was taken into account in computing her net income. The Commissioner determined



that the gain resulted from a distribution in partial liquidation of the corporation, and that it was to be treated as a short-term capital gain, all of which was to be taken into account in computing net income. (R. 24-25.)

The Tax Court affirmed the Commissioner's determination (R. 25-28), four judges dissenting (R. 28-29).

The Circuit Court of Appeals affirmed the decision of the Tax Court, one judge dissenting (R. 39-42).

#### ARGUMENT

The judgment below is correct and is not in conflict with any decision. No other sufficient reason for issuing a writ of certiorari has been suggested by the taxpayer.

(1) The Tax Court's findings show that in 1940 the corporation distributed to the taxpayer certain of its lands in exchange for one-half of its entire stock which the taxpayer surrendered for cancellation. The remainder of the corporation's lands was not distributed and the one-half of the corporation's stock owned by the Austin estate was not surrendered for cancellation but continued to be held by the estate. (R. 22-24.) The distribution to the taxpayer by the corporation was one made "in complete cancellation or redemption of a part of its stock"; it thus fits exactly within the first part of the definition of "amounts distributed in partial liquidation" in Section 115 (i) of

the Internal Revenue Code (Appendix, *infra*)<sup>1</sup> and also within Section 19.115-5 (c) of Treasury Regulations 103 (Appendix, *infra*), which provides that a complete cancellation of a part of the corporate stock may be accomplished, *inter alia*, by the complete retirement of any part of the stock, whether or not *pro rata* among the stockholders. The court below therefore correctly decided that the distribution to the taxpayer was one in partial liquidation within the meaning of Section 115 (i).

Even if it were reasonable to infer from the Tax Court's findings, which it is not, that the distribution was intended to be in effect a complete liquidation as taxpayer contends (Pet. 13-16) rather than a partial liquidation, the lower court would not have been warranted in concluding that Section 115 (i) did not apply. The controlling fact is that the corporation did not cancel all of its stock but only a part of it. The settled construction of the first definition in Section 115 (i) is that it is complete in itself for tax purposes, that no limitations or additional criteria are to be supplied, and that it applies to corporate distributions falling precisely within its terms, even though there was no intent, as such, partly to liquidate the corporation. See *Stern v. Harrison*, 152 F. 2d

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<sup>1</sup> The second part of the statutory definition is not involved here, since, as the Tax Court pointed out (R. 25), no previous or subsequent distributions in cancellation of stock appear to have been made, and hence the distribution to the taxpayer was not one of a series of distributions.

321 (C. C. A. 7th), certiorari denied, 327 U. S. 807; *Yankey v. Commissioner*, 151 F. 2d 650 (C. C. A. 10th); *Citizens & Southern Nat. Bank v. Commissioner*, 136 F. 2d 406 (C. C. A. 5th); *Dodd v. Commissioner*, 131 F. 2d 382 (C. C. A. 5th); *Malone v. Commissioner*, 128 F. 2d 967 (C. C. A. 5th); *Hill v. Commissioner*, 126 F. 2d 570 (C. C. A. 5th); *Alpers v. Commissioner*, 126 F. 2d 58 (C. C. A. 2d); *Amelia H. Cohen Trust v. Commissioner*, 121 F. 2d 689 (C. C. A. 3d); *Hammans v. Commissioner*, 121 F. 2d 4 (C. C. A. 2d); *Commissioner v. Quackenbos*, 78 F. 2d 156 (C. C. A. 2d); *Mittelman v. Commissioner*, 5 T. C. 932, 939-940; *Allport v. Commissioner*, 4 T. C. 401, 403, dismissed and affirmed January 29, 1946 (C. C. A. 7th); *Irvine v. Commissioner*, 46 B. T. A. 246; *Britt v. Commissioner*, 40 B. T. A. 790, 795-796, affirmed on other grounds, 114 F. 2d 10 (C. C. A. 4th); *Salt Lake Hardware Co. v. Commissioner*, 27 B. T. A. 482. See, also, 1 Mertens, *Law of Federal Income Taxation*, Section 9.83.<sup>2</sup> Cf. *Thornton v. Commissioner*, decided January 31, 1947 (C. C. A. 7th) (1947 P-H, par. 72,357).

<sup>2</sup> *Beretta v. Commissioner*, 141 F. 2d 452 (C. C. A. 5th), certiorari denied, 323 U. S. 720, contains language suggesting that an intention to liquidate corporate business is required to make a distribution one in partial liquidation within the meaning of the first definition in Section 115 (i). This view is not consistent with other decisions of the same court, cited above. The *Beretta* opinion cited *Bynum v. Commissioner*, 113 F. 2d 1 (C. C. A. 5th), as support for the view there taken, but the *Bynum* case was not apposite, since it was not concerned with the first definition of partial liquidation in Sec-

As indicated, the taxpayer argues (Pet. 13-16) that the transaction should be treated as a complete liquidation on the basis of what she conceives the intention of the parties to have been. The meaning of the term "complete liquidation," for purposes of taxing the gain on a distribution in complete liquidation, is defined in Section 115 (c) (Appendix, *infra*), and the procedure followed here does not fall within that definition. Moreover, the Tax Court found (R. 27) that the stockholders did not intend to effect a complete liquidation of the corporation and the record fully supports that determination. The Austin estate expressly refused to liquidate the corporation and distribute all its assets. Instead, it redrafted the contract, which taxpayer signed, to provide for only a partial distribution of assets in cancellation of part of the stock. (R. 20.) The final agreement reflects the stockholders' intention. The decision of the court below does not deny that the purpose of the stockholders was to divide completely the corporate assets; it merely declares that the method employed to achieve the purpose

tion 115 (i), but solely with the second definition, in connection with which an intention to liquidate may be pertinent to show that a particular distribution is one of a series in complete cancellation of all the stock. The *Beretta* case, however, correctly decided that there was no partial liquidation in that case, as first defined in Section 115 (i), because there was not a complete cancellation of any part of the stock, but only a reduction in par value of all of the stock.

conformed to the statutory definition of a partial liquidation, rather than that of a complete liquidation.

There is, likewise, no basis for the view that the substance of the transaction was different from its form (Pet. 16-20). None of the cases cited by taxpayer (Pet. 17) are apposite to the facts here. In this case the form selected fully carried out the purposes of the taxpayer and the Austin estate as reflected in their agreement and in the resolutions adopted by the corporation. The fact that the taxpayer, alone of the two stockholders, would have preferred to divide the corporation's assets through the mechanics of a complete liquidation does not demonstrate that the partial liquidation agreed upon amounted in substance to a complete liquidation. Also, since the corporation and its stockholders elected to complete the transaction as a partial liquidation, they are bound to accept the tax consequences of the plan. See *Higgins v. Smith*, 308 U. S. 473, 477-478; *Commissioner v. Moline Properties*, 131 F. 2d 388, 389 (C. C. A. 5th), affirmed, 319 U. S. 436.

(2) Since the distribution to the taxpayer was an amount distributed in partial liquidation as defined in Section 115 (i), it is, as the lower court held, subject to be taxed as provided in Section 115 (c). That is, the lands received by taxpayer are to be treated as received in exchange for the stock surrendered, and the gain thereon

to the extent recognized<sup>3</sup> is to be considered as a short-term capital gain (defined in Section 117 (a) (2) (Appendix, *infra*)) with the result that all of it is to be included in gross income under Section 117 (b) (Appendix, *infra*). All of the cases have construed the language of Section 115 (c) as conclusive that the gain on any distribution in partial liquidation, made prior to 1942, is taxable in its entirety.<sup>4</sup> See, also, Section 19.115-5 (c) of Treasury Regulations 103 (Appendix, *infra*).

The taxpayer's assertion (Pet. 11-13) that this provision of Section 115 (c) was intended to apply, not to *bona fide* cancellations of stock, but solely to distributions of earnings disguised as liquidating distributions, was properly rejected by the lower court.<sup>5</sup> Section 115 (g), rather than Section 115 (c), is the section which is concerned specifically with distributions of earnings in can-

<sup>3</sup> There is no dispute as to the computation of the gain under Section 111 or that all of it is to be recognized under Section 112 (a). The taxpayer's agreed basis for the stock was \$2,750 (R. 18) and the fair market value of the lands received was \$87,802 $\frac{1}{2}$  (R. 22). Her gain was thus \$85,052.

<sup>4</sup> *Stern v. Harrison*, 152 F. 2d 321 (C. C. A. 7th), certiorari denied, 327 U. S. 807; *Yankey v. Commissioner*, 151 F. 2d 650 (C. C. A. 10th); *Malone v. Commissioner*, 128 F. 2d 967 (C. C. A. 5th); *Hill v. Commissioner*, 126 F. 2d 570 (C. C. A. 5th); *Amelia H. Cyphen Trust v. Commissioner*, 121 F. 2d 689 (C. C. A. 3d); *Hammans v. Commissioner*, 121 F. 2d 4 (C. C. A. 2d).

<sup>5</sup> *Thornton v. Commissioner*, decided January 31, 1947 (C. C. A. 7th) (1947 P-H ¶ 72,357) contains language which would appear to afford some basis for this assertion. Examination of the opinion indicates that the statement is dictum and that the decision is based on a strict construction of the language of the statute.

cellation of stock, which are essentially equivalent to a taxable dividend. The contention, moreover, is contrary to the unambiguous language of Section 115 (c), to the regulation, to express rulings in *Stern v. Harrison*, *supra*, and *Hammons v. Commissioner*, *supra*, to the reasoning of the other decisions cited in footnote 4, *supra*, and to statements in H. Rep. No. 2333, 77th Cong., 2d Sess., pp. 49, 93 (1942-2 Cum. Bull. 372, 412, 442-443) and S. Rep. No. 1631, 77th Cong., 2d Sess., p. 116 (1942-2 Cum. Bull. 504, 591), which explain the non-retroactive repeal of Section 115 (c) by Section 147 of the Revenue Act of 1942, c. 619, 56 Stat. 798, as designed to correct inequities, pointing out that under "existing law" gains on distributions in partial liquidation were taxed as short-term capital gains, irrespective of the period the stock was actually held.<sup>6</sup>

Finally, equitable considerations (see Pet. 10-11, 16) would not have justified a construction of the statutory provisions controlling the taxation of the distribution which was directly opposed to, or inconsistent with, the plain meaning of the language used. *Deputy v. du Pont*, 308

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<sup>6</sup> The effect of the 1942 change is that gains on distributions in partial liquidation made in 1942 and subsequent years are treated as are other capital gains. The amount of the gain which is taxable is determined by the period the surrendered stock has been held. Thus, a gain is included in income in its entirety only if the cancelled or redeemed stock has actually been held for the period to qualify it as a short-term capital asset as defined in the Internal Revenue Code.

U. S. 488, 498; *United States v. Emory*, 314 U. S. 423, 430-431.<sup>7</sup> This is particularly true where, as here, Congress itself has declined to change the method of taxing distributions in partial liquidation, except for 1942 and subsequent years, despite the recognized inequities in existing law.

#### CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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MARCH, 1947.

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<sup>7</sup> *Stone v. White*, 301 U. S. 532, cited by the taxpayer (Pet. 10), was concerned with the equitable right of set-off in a suit to recover an erroneously paid tax, a wholly different question from that here.



## APPENDIX

### Internal Revenue Code:

#### SEC. 115. DISTRIBUTIONS BY CORPORATIONS.

\* \* \* \* \*

(c) *Distributions in Liquidation.*—Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112. Despite the provisions of section 117, the gain so recognized shall be considered as a short-term capital gain, except in the case of amounts distributed in complete liquidation. For the purpose of the preceding sentence, “complete liquidation” includes any one of a series of distributions made by a corporation in complete cancellation or redemption of all of its stock in accordance with a bona fide plan of liquidation and under which the transfer of the property under the liquidation is to be completed within a time specified in the plan, not exceeding, from the close of the taxable year during which is made the first of the series of distributions under the plan, (1) three years, if the first of such series of distributions is made in a taxable year beginning after December 31, 1937, or (2) two years,

if the first of such series of distributions was made in a taxable year beginning before January 1, 1938. In the case of amounts distributed (whether before January 1, 1939, or on or after such date) in partial liquidation (other than a distribution to which the provisions of subsection (h) of this section are applicable) the part of such distribution which is properly chargeable to capital account shall not be considered a distribution of earnings or profits.\* \* \*

\* \* \* \* \*

(i) *Definition of Partial Liquidation.*—

As used in this section the term “amounts distributed in partial liquidation” means a distribution by a corporation in complete cancellation or redemption of a part of its stock, or one of a series of distributions in complete cancellation or redemption of all or a portion of its stock.

\* \* \* \* \*

(26 U. S. C. 115.)

SEC. 117. CAPITAL GAINS AND LOSSES.

(a) *Definitions.*—As used in this chapter—

\* \* \* \* \*

(2) *Short-term Capital Gain.*—The term “short-term capital gain” means gain from the sale or exchange of a capital asset held for not more than 18 months, if and to the extent such gain is taken into account in computing net income;

\* \* \* \* \*

(b) *Percentage Taken into Account.*—In the case of a taxpayer, other than a corporation, only the following percentages of the gain or loss recognized upon the sale or

exchange of a capital asset shall be taken into account in computing net income:

100 per centum if the capital asset has been held for not more than 18 months;  
 66 $\frac{2}{3}$  per centum if the capital asset has been held for more than 18 months but not for more than 24 months;  
 50 per centum if the capital assets has been held for more than 24 months.

\* \* \* \* \*

(26 U. S. C. 117.)

Treasury Regulations 103, promulgated under the Internal Revenue Code:

SEC. 19.115-5. *Distributions in liquidation.*—

(a) *General.*—Amounts distributed in complete liquidation of a corporation are to be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation are to be treated as in part or full payment in exchange for the stock so cancelled or redeemed. The gain or loss to a shareholder from a distribution in liquidation is to be determined, as provided in section 111 and section 19.111-1, by comparing the amount of the distribution with the cost or other basis of the stock provided in section 113; but the gain or loss will be recognized only to the extent provided in section 112.

\* \* \* \* \*

(c) *Partial liquidation.*—In the case of amounts distributed in partial liquidation of a corporation, the amount of the loss recognized is subject to the limitations contained in section 117 but the entire amount of the gain recognized shall be considered as a short-term capital gain despite the provi-

sions of section 117.\* The term "amounts distributed in partial liquidation" means a distribution by a corporation in complete cancellation or redemption of a part of its stock, or one of a series of distributions in complete cancellation or redemption of all or a portion of its stock. A complete cancellation or redemption of a part of the corporate stock may be accomplished, for example, by the complete retirement of all the shares of a particular preference or series, or by taking up all the old shares of a particular preference or series and issuing new shares to replace a portion thereof, or by the complete retirement of any part of the stock, whether or not pro rata among the shareholders.

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\*This sentence was amended by T. D. 5230, 1943 Cum. Bull. 299, 308, to conform it to the provisions of the Revenue Act of 1942, but the amendment does not affect the year involved in this case.